Southern Union Company
Department of Telecommunications and Energy
D.T.E. 06-2
Information Request: **DTE-1-14**
January 19, 2006
Person Responsible: Richard N. Marshall

Information Request DTE-1-14

Refer to Exhibit SU-2, Section 4.4. "Financial Statements." Please provide a copy of the financial statements contained in Schedule 4.4.

Response

Please see Attachment DTE-1-14.

## Schedule 4.4

## FINANCIAL STATEMENTS

See attached

KPMG

# RICHARDSON ENERGY MARKETING, LTD.
(a Texas Limited Partnership)

Financial Statements

December 31, 2004 and 2003

(With Independent Auditors' Report Thereon)

KPMG

**KPMG LLP**
2500 D R Horton Tower
301 Commerce Street
Fort Worth, TX 76102

## Independent Auditors' Report

The Partners
Richardson Energy Marketing, Ltd.:

We have audited the accompanying balance sheets of Richardson Energy Marketing, Ltd. (a Texas Limited Partnership) (the Partnership) as of December 31, 2004 and 2003, and the related statements of operations, changes in partners' capital (deficit), and cash flows, for each of the years in the three-year period ended December 31, 2004. These financial statements are the responsibility of the Partnership's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Partnership's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Richardson Energy Marketing, Ltd. as of December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

September 12, 2005

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Balance Sheets

December 31, 2004 and 2003

| **Assets** | | **2004** | **2003** |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents | $ | 1,833,725 | 5,482,969 |
| Receivables (note 2): | | | |
| Trade | | 73,059,421 | 65,115,535 |
| Trade – affiliates (notes 5 and 6) | | 7,448,073 | 6,690,297 |
| Due from brokers (note 4) | | 525,964 | 1,196,709 |
| Due from counterparties (note 4) | | 587,215 | 1,158,005 |
| Total receivables | | 81,620,673 | 74,160,546 |
| Inventories (note 6) | | 179,845 | 123,900 |
| Prepaid expenses | | 16,941 | 8,075 |
| Marketable securities (note 4) | | 500 | 44,600 |
| Total current assets | | 83,651,684 | 79,820,090 |
| Property, plant, and equipment, at cost: | | | |
| Land | | 55,523 | 55,523 |
| Leasehold improvements | | 107,321 | 107,321 |
| Pipeline equipment | | 1,457,648 | 1,457,648 |
| Office equipment | | 660,599 | 649,669 |
| Transportation equipment | | 29,406 | 25,439 |
| | | 2,310,497 | 2,295,600 |
| Less accumulated depreciation | | 1,532,311 | 1,437,330 |
| Net property, plant, and equipment | | 778,186 | 858,270 |
| Other assets (note 4) | | 25,000 | 422,800 |
| | $ | 84,454,870 | 81,101,160 |
| **Liabilities and Partners' Capital (Deficit)** | | | |
| Current liabilities: | | | |
| Bank overdraft | $ | 531,917 | 1,146,697 |
| Accounts payable – trade | | 19,872,954 | 16,162,841 |
| Accounts payable – affiliates (note 6) | | 54,839,890 | 54,883,946 |
| Due to counterparties (note 4) | | 352,502 | 1,081,284 |
| Accrued liabilities (note 5) | | 1,572,953 | 1,499,045 |
| Total current liabilities | | 77,170,216 | 74,773,813 |
| Other long-term liablities (note 5) | | 8,963,799 | 8,852,490 |
| Partners' capital (deficit) | | (1,679,145) | (2,525,143) |
| Commitments and contingencies (notes 5, 7, and 8) | | | |
| | $ | 84,454,870 | 81,101,160 |

See accompanying notes to financial statements.

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Statements of Operations

Years ended December 31, 2004, 2003 and 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Natural gas liquids and natural gas sales (notes 4 and 6) | $ 831,381,456 | 787,001,948 | 579,239,831 |
| Cost of sales (note 6) | 825,925,487 | 785,204,597 | 581,930,743 |
| (Gain) loss on derivative instruments, net (note 4) | 1,341,449 | (2,579,489) | 5,217,010 |
| General and administrative expenses (notes 5 and 6) | 3,658,185 | 3,596,230 | 3,463,878 |
| Operating income (loss) | 456,335 | 780,610 | (11,371,800) |
| Other income (expense): | | | |
| Interest income | 399,938 | 165,242 | 274,923 |
| Interest expense – affiliates (note 6) | (242) | (129,240) | (115,764) |
| Other, net | (10,033) | 3,610 | (26,930) |
| Other income, net | 389,663 | 39,612 | 132,229 |
| Net income (loss) | $ 845,998 | 820,222 | (11,239,571) |

See accompanying notes to financial statements.

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Statements of Changes in Partners' Capital (Deficit)

Years ended December 31, 2004, 2003 and 2002

| | | General Partner | Limited Partner | Total |
|---|---|---|---|---|
| Balance at December 31, 2001 | $ | 224,001 | 7,670,205 | 7,894,206 |
| Net loss | | (112,396) | (11,127,175) | (11,239,571) |
| Balance at December 31, 2002 | | 111,605 | (3,456,970) | (3,345,365) |
| Net income | | 8,202 | 812,020 | 820,222 |
| Balance at December 31, 2003 | | 119,807 | (2,644,950) | (2,525,143) |
| Net income | | 8,460 | 837,538 | 845,998 |
| Balance at December 31, 2004 | $ | 128,267 | (1,807,412) | (1,679,145) |

See accompanying notes to financial statements.

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)
Statements of Cash Flows
Years ended December 31, 2004, 2003 and 2002

| | | 2004 | 2003 | 2002 |
|---|---|---|---|---|
| Cash flows from operating activities: | | | | |
| Net income (loss) | $ | 845,998 | 820,222 | (11,239,571) |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | | | |
| Depreciation | | 94,981 | 97,737 | 96,978 |
| Bad debt expense | | 12,807 | 1,250 | 240,707 |
| (Gain) loss on derivative instruments, net | | 587,518 | (2,515,893) | 6,500,499 |
| Changes in assets and liabilities: | | | | |
| Trade receivables | | (7,956,693) | (2,375,792) | (21,176,762) |
| Trade receivables – affiliates | | (757,776) | (247,358) | (816,653) |
| Accrued interest receivable – affiliates | | — | 14,097 | 120,703 |
| Due from counterparties | | (782,973) | 2,882,816 | 1,886,221 |
| Inventories | | (55,945) | (39,290) | 338,765 |
| Prepaid expenses | | (8,866) | (816) | 11,357 |
| Other assets | | 397,800 | 112,200 | (510,000) |
| Accounts payable – trade | | 3,710,113 | (9,284,002) | (1,173,015) |
| Accounts payable – affiliates | | (44,056) | 14,287,863 | 13,102,154 |
| Due to counterparties | | (63,792) | (181,227) | 116,334 |
| Accrued liabilities | | 73,908 | 692,647 | (318,743) |
| Accrued interest payable – affiliates | | — | (43,356) | 43,356 |
| Other long-term liabilities | | 111,309 | 102,780 | 859,067 |
| Net cash provided by (used in) operating activities | | (3,835,667) | 4,323,878 | (11,918,603) |
| Cash flows from investing activities: | | | | |
| Advances on note receivable – affiliates | | — | (58,268,422) | (231,941,705) |
| Receipts on note receivable – affiliates | | — | 62,753,900 | 249,756,405 |
| Purchases of property, plant and equipment | | (43,192) | (55,495) | (8,059) |
| Disposals of property, plant and equipment | | 28,295 | 11,091 | — |
| Change in due from brokers | | 670,745 | (1,046,244) | 4,977,951 |
| Purchases of marketable securities | | (8,281) | (253,306) | — |
| Settlement of futures, net | | 109,036 | (474,032) | (7,581,528) |
| Proceeds from sale of marketable securities | | 44,600 | 115,900 | — |
| Net cash provided by investing activities | | 801,203 | 2,783,392 | 15,203,064 |
| Cash flows from financing activities: | | | | |
| Change in bank overdraft | | (614,780) | 506,097 | (5,414,859) |
| Proceeds from note payable – affiliates | | 32,702,336 | 80,710,427 | 49,058,850 |
| Payments on note payable – affiliates | | (32,702,336) | (89,808,664) | (39,960,613) |
| Net cash provided by (used in) financing activities | | (614,780) | (8,592,140) | 3,683,378 |
| Net change in cash and cash equivalents | | (3,649,244) | (1,484,870) | 6,967,839 |
| Cash and cash equivalents at beginning of year | | 5,482,969 | 6,967,839 | — |
| Cash and cash equivalents at end of year | $ | 1,833,725 | 5,482,969 | 6,967,839 |

Supplemental disclosure of cash flow information:
Cash paid for interest in 2004, 2003, and 2002 totaled $242, $172,596, and $72,408, respectively.

See accompanying notes to financial statements.

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Notes to Financial Statements

December 31, 2004 and 2003

## (1) Organization and Description of Business

Richardson Energy Marketing, Ltd. (the Partnership), a Texas limited partnership formed on March 1, 1993, sells natural gas and natural gas liquids to a variety of customers including power generation companies, utilities, energy marketers, and industrial users located primarily in the southwestern United States. The Partnership seeks to manage commodity price risk through a risk management program and credit risk by selling to reliable and creditworthy customers. The Partnership purchases a significant portion of its natural gas and natural gas liquids from affiliates, including Sid Richardson Energy Services, Ltd. and subsidiaries (SRES), an affiliate under common control.

## (2) Summary of Significant Accounting Policies and Practices

### *(a) Basis of Presentation*

The accompanying financial statements were prepared in accordance with accounting principles generally accepted in the United States of America. Net income or loss is credited or charged to the partners' capital accounts in accordance with their respective percentage interest as stated in the partnership agreement. The Partnership is permitted to make distributions based on the availability of distributable funds as determined by the General Partner. The allocation of distributions is based on each partner's interests pursuant to the partnership agreement, consistent with the allocation of net income or loss.

### *(b) Use of Estimates*

The Partnership has made certain estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting policies generally accepted in the United States of America. Although the Partnership believes the estimates are appropriate, actual results could differ from those estimates.

### *(c) Cash and Cash Equivalents*

The Partnership considers investments in highly liquid financial instruments with an original maturity of three months or less at the date of purchase to be cash equivalents. Cash and cash equivalents include $910,004 and $3,219,418 of money market investments at December 31, 2004 and 2003, respectively.

### *(d) Significant Suppliers and Concentrations of Credit Risk*

SRES, an affiliate under common control, is the supplier of a significant portion of the Partnership's inventories of natural gas and natural gas liquids. The Partnership believes that it could either replace purchases from SRES with purchases from other sellers of natural gas and natural gas liquids or simultaneously reduce sales commitments to offset the loss of SRES as a supplier without a material adverse effect on the Partnership's results of operations.

Financial instruments, which potentially subject the Partnership to concentrations of credit risk, consist primarily of cash and cash equivalents, accounts receivable and derivative financial instruments. The Partnership invests cash and cash equivalents in money market accounts with highquality institutions. The Partnership derives its revenues and accounts receivables from customers primarily in the natural gas and utilities industries. Since these customers could be similarly affected by changes in the economy, industries and other conditions, the industry concentrations could potentially affect the Partnership's overall exposure to credit risk – either positively or negatively. However, the exposure to credit risk is mitigated by the creditworthiness of the Partnership's customer base. The Partnership's accounts receivable primarily consist of mid to large domestic customers with credit ratings of investment grade or better. The Partnership screens the list of derivative financial instrument counterparties by evaluating the ability of each counterparty to perform under the terms of the derivatives agreement. The Partnership maintains trading relationships with counterparties that include U.S. broker-dealers and other financial institutions.

### *(e) Reserves for Uncollectible Receivables*

The Partnership extends credit to customers and other parties in the normal course of business. The Partnership has established various procedures to manage its credit exposure, including initial credit approvals, credit limits and rights of offset. The Partnership also uses prepayments and guarantees to limit credit risk to ensure that management's established credit criteria are met. The Partnership records reserves for uncollectible receivables on a specific identification basis since there is not a large volume of uncollectible receivables. During the years ended December 31, 2004, 2003 and 2002, the Partnership recorded reserves and wrote off uncollectible receivables of $12,807, $1,250 and $240,707, respectively. The amounts reserved and written off during 2002 primarily related to one customer. No reserves for uncollectible receivables were recorded as of December 31, 2004 and 2003.

### *(f) Inventories*

Inventories consist primarily of natural gas liquids and are stated at the lower of cost or market value. Cost is determined using the first-in, first-out method (FIFO).

### *(g) Property, Plant and Equipment*

Property, plant and equipment are recorded at cost. The Partnership charges repairs and maintenance against income when incurred and capitalizes renewals and betterments, which extend the useful life or expand the capacity of the assets. The Partnership calculates depreciation on the straight-line method over the following estimated useful lives: pipeline equipment – 25 years; leasehold improvements – amortized over the shorter of the lease term or estimated useful life of the asset - 10 years; office equipment – 10 years; transportation equipment – 3 years.

### *(h) Impairment of Long-Lived Assets*

In accordance with Statement of Financial Accounting Standard ("SFAS") No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Partnership evaluates its long-lived assets for impairment when events or changes in circumstances indicate, in the Partnership's judgment, that the carrying value of such asset may not be recoverable. The determination of whether impairment has occurred is based on the Partnership's estimate of undiscounted future cash flows attributable to the assets as compared to the carrying value of the assets. If impairment has occurred, the amount of impairment recognized is determined by estimating the fair value of the assets and recording a provision for the amount by which the carrying value exceeds fair value. For assets identified as held for sale, the carrying value of these assets is compared to the estimated fair value, less the cost to sell, to determine if an impairment has occurred. An asset is no longer depreciated while it is held for sale. Until the assets are disposed of, an estimate of the fair value is re-evaluated when related events or circumstances change.

When determining whether impairment of one of the Partnership's long-lived assets has occurred, the Partnership must estimate the undiscounted cash flows attributable to its assets or asset groups. Such an estimate of cash flows is based on assumptions regarding future prices for natural gas liquids product and natural gas. Projections of future commodity prices are inherently subjective and contingent upon a number of factors, many of which are difficult to forecast. Any significant variance in any of these assumptions or factors could materially affect future cash flows. The Partnership has reviewed its long-lived assets for impairments and has not identified any such impairments.

*(i)* ***Asset Retirement Obligation***

SFAS No. 143, *Accounting for Asset Retirement Obligations*, (SFAS No. 143) was issued in June 2001. The Partnership adopted SFAS No. 143 beginning January 1, 2003. This statement requires entities to record the fair value of a liability for legal obligations associated with the retirement obligations of tangible long-lived assets in the period in which the obligation is incurred and can be reasonably estimated. When the liability is initially recorded, a corresponding increase in the carrying amount of the related long-lived asset is recorded. Over time, accretion of the liability is recognized each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss on settlement.

Under the implementation guidelines of SFAS No. 143, the Partnership has reviewed its long-lived assets and lease arrangements for asset retirement obligation (ARO) liabilities and identified any such liabilities. These liabilities include AROs related to (i) rights-of-way and easements over property not owned by the Partnership, (ii) leases of certain currently operated facilities and (iii) regulatory requirements triggered by the abandonment or retirement of certain of these assets.

The Partnership's rights under its easements are renewable or perpetual and retirement action, if any, is required only upon non-renewal or abandonment of the easements. The Partnership currently expects to continue to use or renew all such easement agreements and to use these properties for the foreseeable future. Similarly, under certain leases of currently operated facilities, retirement action is only required upon termination of these leases and the Partnership does not expect termination in the foreseeable future. Accordingly, the Partnership is unable to reasonably estimate and record liabilities for its obligations that fall under the provisions of SFAS No. 143 because it does not believe that any of the applicable assets will be retired or abandoned in the foreseeable future. The Partnership will record AROs in the period in which the obligation may be reasonably estimated.

*(j) Gas Imbalances*

Quantities of natural gas over or under delivered related to gas balancing agreements are recorded monthly as receivables or payables using weighted average prices at the time of the imbalance. These imbalances are settled with deliveries of natural gas in future periods, usually within one month. The Partnership had imbalance payables of $493,743 and $2,212,436 at December 31, 2004 and 2003, respectively, which are carried at the fair value of these imbalances. The Partnership had imbalance receivables of $1,494,488 and $2,173,438 at December 31, 2004 and 2003, respectively, which are carried at the lower of cost or market value. Imbalance receivables are included in *Trade receivables* and imbalance payables are included in *Accounts payable – trade* on the accompanying balance sheets.

*(k) Revenue and Cost of Sales Recognition*

Revenue and the related cost of sales for natural gas and natural gas liquids are recognized in the period when the physical product is delivered to the customer at the contractually agreed-upon price and title is transferred. Cost of sales primarily includes the cost of purchased natural gas and natural gas liquids and related transportation expenses.

The Partnership accounts for sale and purchase arrangements on a gross basis in the accompanying statements of operations as *Natural gas liquids and natural gas sales* and *Cost of sales*, respectively. Contractual arrangements establish the purchase of natural gas and natural gas liquids at specified locations and the sale at different locations on the same or other specified dates. Both purchase and sale transactions require physical delivery of the natural gas and natural gas liquids. The transfer of ownership is evidenced by the purchaser's assumption of title, price risk, credit risk, counterparty nonperformance risk, environmental risk, and transportation scheduling.

*(l) Income Taxes*

The Partnership is not a taxable entity for Federal income tax purposes. As such, the Partnership does not directly pay Federal income tax. The Partnership's taxable income or loss, which may vary substantially from the net income or loss reported in the statements of operations, is includable in the Federal income tax return of each partner. Consequently, no income taxes have been reflected in the accompanying financial statements.

*(m) Derivative Financial Instruments and Risk Management Activities*

The Partnership markets natural gas and natural gas liquids and manages associated risks using derivative financial instruments. The Partnership accounts for derivative financial instruments in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended (SFAS No. 133). Derivative financial instruments subject the Partnership to off-financial statement risk. Derivative financial instruments involve not only the risk of dealing with counterparties and their ability to meet the terms of the contracts but also the risk associated with unmatched positions and market fluctuations. Notional, face or contract amounts often are used to express the volume of these transactions, but the amounts potentially subject to credit risk are much smaller.

Under SFAS No. 133, the Partnership is required to record derivative financial instruments at fair value. The fair value of derivative financial instruments is determined by commodity exchange prices, over-the-counter quotes, volatility, time value, counterparty credit and the potential impact on market prices of liquidating positions in an orderly manner over a reasonable period of time under current market conditions. The majority of the Partnership's fair values are based on actual market prices. Under SFAS No. 133, market value changes result in a change in the fair value of derivative financial instruments. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding it. If the derivative instrument does not qualify or is not designated as part of a hedging relationship, changes in fair value of the derivative are recognized in earnings as they occur. Commodity price volatility may have a significant impact on the gain or loss in any given period.

To minimize the risk of price fluctuations in natural gas and natural gas liquids, the Partnership uses various derivative financial instruments to manage risks associated with anticipated purchases and sales of natural gas and natural gas liquids. In order to account for these derivative financial instruments as hedges, SFAS No. 133 requires an entity to formally document all relationships between hedging instruments and hedged items, as well as risk management objectives, strategies for undertaking various hedge transactions and methods for assessing and testing hedge effectiveness and ineffectiveness. Specific assets, liabilities, firm commitments or forecasted transactions must be designated as hedged items. The effectiveness of hedging relationships, both at the inception of the hedge and on an ongoing basis, must be assessed. Since the Partnerships' accounting records historically have been prepared on the accrual basis of accounting in accordance with practices permitted for income tax purposes, the Partnership has not met the documentation requirements of SFAS No. 133. Therefore, changes in fair value for these derivative financial instruments are recognized in earnings as they occur and are reported net in *Gain (loss) on derivative instruments, net* in the accompanying statements of operations and in *Due from/Due to counterparties* in the accompanying balance sheets.

The Partnership also trades various derivative financial instruments to take advantage of pricing anomalies among derivative financial instruments related to natural gas and natural gas liquids. Changes in fair value for these derivative financial instruments are recognized in earnings as they occur and are reported net in *Gain (loss) on derivative instruments, net* in the accompanying statements of operations and in *Due from brokers* and *Marketable securities* in the accompanying balance sheets.

***(n) Contracts for Physical Purchases and Sales***

The Partnership's contracts for the physical purchase and sale of natural gas and natural gas liquids are derivatives under SFAS No. 133, since the underlying natural gas and natural gas liquids are commodities readily convertible to cash – thereby meeting the net settlement provision of SFAS No. 133. However, the contracts do not provide for a net settlement in cash, nor do they provide for any settlement mechanism other than the physical delivery of the underlying natural gas and natural gas liquids. These contracts would therefore have qualified for the normal purchases and normal sales exemption under SFAS No. 133 had the Partnership documented its designation of the contracts as normal purchases or normal sales. In this case, the contracts would have been exempt from fair value accounting treatment and not treated as derivatives. Since the Partnerships' accounting records historically have been prepared on the accrual basis of accounting in accordance with practices permitted for income tax purposes, the Partnership has not met the documentation requirements of SFAS No. 133. Therefore, the Partnership's open contracts for the physical purchase and sale of natural gas and natural gas liquids are reported at fair value. The Partnership recorded mark-to-market adjustments for these contracts of $753,931, ($63,596) and ($1,283,489) for the years ended December 31, 2004, 2003 and 2002, respectively, and reported such adjustments in *Natural gas liquids and natural gas sales* in the accompanying statements of operations.

The Partnership considered the following EITF conclusions in determining whether to present revenues and cost of sales related to settled contracts on a gross or net basis in the accompanying statements of operations: EITF Issue No. 99-19, *"Reporting Revenue Gross as a Principal versus Net as an Agent"*; EITF Issue No. 02-03, *"Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities";* and EITF Issue No. 03-11, *"Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not 'Held for Trading Purposes' as Defined in EITF Issue No. 02-3"* (EITF 03-11). EITF 03-11 provides that it is a matter of judgment in the context of relevant facts and circumstances of whether realized gains and losses on physically settled derivative contracts not "held for trading purposes" should be reported in the statements of operations on a gross or net basis.

The Partnership has determined that these contracts are not held for trading purposes since title, price risk, credit risk, counterparty nonperformance risk, environmental risk, and transportation scheduling pass from seller to buyer when the natural gas and natural gas liquids are physically delivered. The Partnership assumes these risks when it purchases natural gas and natural gas liquids and transfers these risks to buyers when it sells the natural gas and natural gas liquids in the context of the ordinary business cycle of the Partnership. Revenues and cost of sales are therefore reported on a gross basis for settled contracts in the accompanying statements of operations.

***(o) Comprehensive Income***

Comprehensive income includes net income (loss) and other comprehensive income (loss), which may include items such as unrealized holding gains and losses on available-for-sale securities, gains and losses on derivative financial instruments accounted for as a cash flow hedge, adjustments to minimum pension liabilities, or foreign currency translation adjustments. The Partnership did not have any items resulting in a difference between net income (loss) and other comprehensive income (loss) during the years ended December 31, 2004, 2003 and 2002.

***(p) Defined Benefit Plans***

The Partnership has a defined benefit retirement plan covering substantially all of its employees and also has a nonqualified defined benefit plan covering certain key executives. The benefits under both plans are based upon years of service and compensation during the ten calendar years before employment ceases. The Partnership computes pension expense for the defined benefit retirement plan and costs associated with the nonqualified defined benefit plan in accordance with SFAS No. 87, *Employers' Accounting for Pensions*.

*(q)* ***Contingencies and Environmental Costs***

The Partnership records a liability for loss contingencies arising from claims, assessments, litigation, fines, and penalties in the financial statements when a loss is known or considered probable and the amount can be reasonably estimated. The Partnership reviews these estimates each accounting period as additional information is known and adjusts the loss accrual when appropriate. If the loss is not probable or cannot be reasonably estimated, a liability is not recorded in the financial statements.

Environmental expenditures are expensed or capitalized as appropriate, depending on the nature of the expenditures and their future economic benefit. Expenditures that relate to an existing condition caused by past operations that do not contribute to current or future revenue generation are expensed. Liabilities for these expenditures are recorded on an undiscounted basis (or discounted when the obligation can be settled at fixed and determinable amounts) when environmental assessments or clean-ups are probable and the costs can be reasonably estimated. For years ended December 31, 2004, 2003 and 2002, such expenditures were not significant.

*(r)* ***Recently Issued Accounting Standards***

In November 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 151, *Inventory Costs* (SFAS No. 151). This statement amends the guidance in Accounting Research Bulletin No. 43 to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material. SFAS No. 151 requires that abnormal amounts of those items be recognized as current-period charges regardless of whether they meet the criteria set forth in the earlier accounting guidance. The statement is effective for fiscal years beginning after June 15, 2005 but earlier adoption is permitted. The adoption of SFAS No. 151 is not expected to have a significant impact on the Partnership's financial statements.

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets* (SFAS No. 153). This statement amends the guidance in Accounting Principles Board opinion No. 29 to require that all exchanges of nonmonetary assets be recorded at the fair value of the assets exchanged except where a nonmonetary exchange has no commercial substance. The statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The adoption of SFAS No. 153 is not expected to have a significant impact on the Partnership's financial statements.

In March 2005, the FASB issued FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143* (FIN 47), which clarifies the accounting for conditional asset retirement obligations as used in SFAS No. 143, *Accounting for Asset Retirement Obligations*. A conditional asset retirement obligation is an unconditional legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of an entity. An entity is required to recognize a liability for the fair value of a conditional asset retirement obligation under SFAS No. 143 if the fair value of the liability can be reasonably estimated. FIN 47 permits, but does not require, restatement of interim financial information. The provisions of FIN 47 are effective for reporting periods ending after December 15, 2005. The Partnership has not yet assessed the impact of adopting FIN 47 on its financial statements.

## (3) Fair Value of Financial Instruments

The Partnership has estimated the fair value of the Partnership's financial instruments using available market information and valuation methodologies. Considerable judgment is required to develop the estimates of fair value. Estimates of fair value are not necessarily indicative of the amount the Partnership could realize upon the sale or refinancing of such financial instruments.

The carrying amounts of the Partnership's cash and cash equivalents, receivables, and payables approximate fair value due to the short-term maturities of these assets and liabilities. Derivative financial instruments used for trading and risk management activities are included in assets or liabilities at fair value.

## (4) Derivative Financial Instruments

The Partnership uses derivative financial instruments both to manage commodity price risk and to take advantage of pricing anomalies among derivative financial instruments related to natural gas and natural gas liquids. All transactions in derivative financial instruments are governed by written risk management guidelines that have been approved by senior management – including the appointment of a senior risk compliance officer to oversee compliance with the guidelines. The Partnership conducts credit reviews on all counterparties and requires collateral as necessary. The Partnership's swap agreements generally allow for offset of positive and negative exposures. The Partnership is subject to margin deposit requirements for over-the-counter ("OTC") agreements with non-bank counterparties and for New York Mercantile Exchange ("NYMEX") positions.

The use of derivative financial instruments may expose the Partnership to the risk of financial loss in certain circumstances, including instances when the Partnership's equity volumes are less than expected; the Partnership's customers fail to purchase or deliver the contracted quantities of natural gas or natural gas liquids; or the Partnership's OTC counterparties fail to perform. To the extent that the Partnership engages in risk management activities, it may be prevented from realizing the benefits of favorable price changes in the physical market. However, the Partnership is similarly insulated against decreases in prices.

The objective of the Partnership's market risk management program is to protect profit margins by managing the price risk associated with the Partnership's marketing of natural gas and natural gas liquids. This risk primarily relates to fixed and floating price purchase and sale commitments, the value of storage inventories and exposure to physical market price volatility.

The Partnership uses the following derivative instruments in its market risk management and derivatives trading program:

- The Partnership uses a combination of fixed price forward contracts, exchange-traded futures and options, fixed for floating index swaps, basis swaps and OTC options to accomplish the risk management objective. These derivative financial instruments allow the Partnership to preserve value and protect margins because changes in the value of the derivative financial instruments offset corresponding changes in the physical market.
- The Partnership also uses derivative financial instruments to reduce basis risk. Basis is the difference in price between the physical commodity and the price of the futures contract used to manage risk.

Basis risk is the risk that an adverse change in the futures market will not be completely offset by an equal and opposite change in the cash price of the physical commodity. For natural gas, basis risk exists primarily due to price differentials between cash market delivery locations and futures contract delivery locations.

- The Partnership enters into futures transactions traded on the NYMEX and through OTC swaps and options with various counterparties, consisting primarily of financial institutions and other natural gas companies. The Partnership conducts a credit review of OTC counterparties and has agreements with many of these parties that contain collateral requirements. The Partnership generally uses standardized swap agreements that allow for offset of positive and negative OTC exposures. OTC exposure is marked-to-market daily for the credit review process. The Partnership's exposure to OTC credit risk is reduced by its ability to require a margin deposit from its counterparties based upon the mark-to-market value of their net exposure. The Partnership is also subject to margin deposit requirements under these same agreements and under margin deposit requirements for its NYMEX transactions. At December 31, 2004, the Partnership had posted $366,525 in margin deposit requirements for its NYMEX transactions with various brokers. Such deposits are reported in *Due from brokers* in the accompanying balance sheets. At December 31, 2003, the Partnership had posted $397,800 in margin deposit requirements for OTC transactions with counterparties. Such deposits are reported in *Other assets* in the accompanying balance sheets.

The following table summarizes information about the derivative instruments used in the market risk management and derivatives trading program as reported in the accompanying balance sheets and statements of operations:

| | | December 31, 2004 | December 31, 2003 |
|---|---|---|---|
| Derivative assets: | | | |
| Due from brokers | $ | 216,091 | 476,860 |
| Marketable securities | | 500 | 44,600 |
| Due from counterparties | | 587,215 | 1,158,005 |
| Derivative liabilities: | | | |
| Due to counterparties | | (352,502) | (1,081,284) |
| Net derivative assets | $ | 451,304 | 598,181 |

| | | Year Ended December 31, 2004 | Year Ended December 31, 2003 | Year Ended December 31, 2002 |
|---|---|---|---|---|
| Natural gas liquids and natural gas sales | $ | 753,931 | (63,596) | (1,283,489) |
| Gain (loss) on derivative instruments, net | | (1,341,449) | 2,579,489 | (5,217,010) |
| Net derivative gains (losses) | $ | (587,518) | 2,515,893 | (6,500,499) |

## (5) Retirement Plans for Employees

*Defined Benefit Plans*

The Partnership participates in a single employer, as a member of a control group, defined benefit retirement plan (the Plan) which covers substantially all of its employees as well as certain employees of affiliates as defined by the Plan. The Plan is sponsored by the Partnership and certain affiliates and is subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA). In addition, the Partnership maintains a nonqualified defined benefit plan (the Restoration Plan) covering certain key executives.

The following table sets forth the benefit obligations, fair value of plan assets, and funded status at December 31, 2004 and 2003:

| | | Plan benefits | | Restoration Plan benefits | |
|---|---|---|---|---|---|
| | | 2004 | 2003 | 2004 | 2003 |
| Projected benefit obligation | $ | 6,874,925 | 6,608,744 | 4,576,787 | 5,106,758 |
| Fair value of plan assets | | 4,600,864 | 3,764,546 | - | - |
| Funded status | $ | (2,274,061) | (2,844,198) | (4,576,787) | (5,106,758) |
| Amounts recognized in the balance sheets consist of: | | | | | |
| Other long-term liabilities | $ | (1,539,272) | (1,336,540) | (7,424,527) | (7,515,950) |

The accumulated benefit obligation for the Plan was $4,809,019 and $4,463,036 at December 31, 2004 and 2003, respectively. The accumulated benefit obligation for the Restoration Plan was $3,811,468 and $4,199,715 at December 31, 2004 and 2003, respectively.

Net periodic benefit cost for the years ended December 31, 2004, 2003 and 2002 was as follows:

| | | Plan benefits | | | Restoration Plan benefits | | |
|---|---|---|---|---|---|---|---|
| | | 2004 | 2003 | 2002 | 2004 | 2003 | 2002 |
| Service cost | $ | 515,959 | 370,009 | 324,930 | 244,245 | 134,016 | 453,426 |
| Interest cost | | 413,046 | 325,283 | 294,857 | 319,172 | 293,669 | 532,162 |
| Expected return on assets | | (301,163) | (263,342) | (281,320) | - | - | - |
| Recognized actuarial loss | | 84,678 | 15,638 | - | (189,851) | (307,504) | - |
| Net periodic benefit cost | $ | 712,520 | 447,588 | 338,467 | 373,566 | 120,181 | 985,588 |

The Partnership contributed $509,788 to the Plan during 2004. No amounts were contributed during 2003 and 2002. The Plan paid $31,121 in benefits each year to its participants during 2004, 2003 and 2002, respectively.

The Partnership paid $464,989 in benefits each year to participants of the Restoration Plan during 2004, 2003 and 2002, respectively.

Weighted-average assumptions used to determine benefit obligations and net benefit cost for the years ended December 31, 2004, 2003 and 2002 were as follows:

| | Plan benefits | | | Restoration Plan benefits | | |
|---|---|---|---|---|---|---|
| | 2004 | 2003 | 2002 | 2004 | 2003 | 2002 |
| Discount rate | 5.75% | 6.25% | 6.75% | 5.75% | 6.25% | 6.75% |
| Expected long-term rate of return on plan assets | 8.00% | 8.00% | 8.00% | 0.00% | 0.00% | 0.00% |
| Rate of compensation increase | 5.00% | 5.50% | 5.50% | 5.00% | 5.50% | 5.50% |

The Plan's expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The return is based exclusively on the Plan's historical returns, without adjustments.

The Plan's investment policy governs how assets are invested. The policy is designed to maximize overall return potential while minimizing the risk of loss. The policy permits designated investment managers to invest in mutual funds, equities, bonds and debt instruments to establish a diversified investment portfolio. Asset allocations are reviewed with investment managers at least annually and more often when it appears that market trends might materially change. The weighted-average asset allocation of the Partnership's Plan assets at December 31, 2004 and 2003 were as follows:

| | Plan Assets at December 31 | |
|---|---|---|
| **Asset Category** | 2004 | 2003 |
| Equity securities | 58% | 56% |
| Debt securities | 13% | 16% |
| Other | 29% | 28% |
| Total | 100% | 100% |

The Partnership does not expect to make any contributions to the Plan during 2005.

The Plan and the Partnership on behalf of the Restoration Plan expect to pay the following benefits in future periods:

| | | Plan | Restoration Plan |
|---|---|---|---|
| Years Ending December 31: | | | |
| 2005 | $ | 1,708,047 | 1,176,327 |
| 2006 | | 26,865 | 8,444 |
| 2007 | | 37,366 | 10,912 |
| 2008 | | 47,373 | 12,973 |
| 2009 | | 387,772 | 43,751 |
| 2010 – 2014 | | 877,562 | 162,533 |

The expected benefits are based on the same assumptions used to measure the Partnership's benefit obligation at each year end and include estimated future employee service. See note (6) for information regarding allocations to affiliates of a portion of these costs.

On January 1, 2005, the Plan was amended to modify benefits for participants who did not meet certain age and service criteria as of that date. The amendments primarily reduced the benefit formula applicable to these participants, eliminated disability benefits previously provided under the Plan, and modified the payment options available for amounts earned under the Plan after December 31, 2004.

*Defined Contribution Plan*

The Partnership also has a 401(k) defined contribution plan to permit participant contributions on a pre-tax basis. This plan is also subject to the provisions of ERISA. The plan allows eligible employees to contribute up to the maximum IRS limits $13,000, $12,000 and $11,000 in 2004, 2003 and 2002, respectively. The Partnership matches the first 4% of the employee's annual compensation on a dollar for dollar basis, up to a maximum of $5,000 per year per employee. Contributions made to this plan by the Partnership in 2004, 2003 and 2002 were approximately $85,000, $82,000 and $76,000, respectively, and are included in *General and administrative expenses* in the accompanying statements of operations.

**(6) Related Party Transactions**

The Partnership purchases natural gas and natural gas liquids from SRES and other affiliates at quoted market prices at the point of delivery. The Partnership uses affiliate-owned facilities to process, treat and transport a portion of its natural gas. During 2004, 2003 and 2002, the Partnership's purchases from SRES and other affiliates amounted to approximately $647,478,000, $598,564,000 and $367,972,000, respectively. During the Partnership's normal business cycle, these amounts become a component of cost of sales and are reported in *Cost of sales* in the accompanying statements of operations, and unsold amounts become part of *Inventories* in the accompanying balance sheets. Amounts owed to affiliates for purchases of natural gas and natural gas liquids are included in *Accounts payable – affiliates* in the accompanying balance sheets.

The Partnership also sells natural gas to certain affiliates at quoted market prices at the point of delivery. During 2004, 2003 and 2002, the Partnership's sales to affiliates amounted to approximately $31,056,000, $30,279,000 and $17,502,000, respectively. Revenues from sales to affiliates are reported in *Natural gas liquids and natural gas sales* in the accompanying statements of operations and the corresponding receivables are reported in *Trade receivables – affiliates* in the accompanying balance sheets.

The Partnership shares certain common administrative services, facilities and office space with affiliates. During 2004, 2003 and 2002, affiliates allocated approximately $156,000, $155,000 and $308,000, respectively, to the Partnership for its portion of these expenses. These allocations are reflected as an increase in *General and administrative expenses* in the accompanying statements of operations. Employees of the Partnership also provide services to other affiliates. During 2004, 2003 and 2002, the Partnership allocated $3,273,423, $2,876,537 and $2,451,342, respectively, to affiliates for their portion of these employees' salaries, benefits, pension expenses, and other related costs. Such allocations are reflected as a reduction of *General and administrative expenses* in the accompanying statements of operations.

During 2004, 2003 and 2002, the Partnership borrowed and repaid $2,000,119, $65,557,514 and $39,960,613, respectively, under a note agreement with an affiliate. The note bore interest at an agreed-upon variable rate and matured on demand or February 2005. Related interest expense is included in *Interest expense – affiliates* in the accompanying statements of operations. There were no amounts outstanding under this agreement at December 31, 2004 and 2003.

The Partnership has an unsecured revolving promissory note payable to an affiliate. The note payable is due on demand or June 7, 2006 and bears interest at an agreed-upon variable rate. Interest is due quarterly. The Partnership borrowed $30,702,217, $15,152,913 and $9,098,237 under this note payable during 2004, 2003 and 2002, respectively. The Partnership repaid $30,702,217 and $24,251,150 under this note payable during 2004 and 2003, respectively. No amounts were outstanding at December 31, 2004 and 2003. Interest expense incurred under this note arrangement is reflected in *Interest expense – affiliates* in the accompanying statements of operations.

## (7) Leases

The Partnership has an operating lease for office space that expires in 2007. The lease contains a renewal option for an additional two year term and requires the Partnership to pay for its portion of the property's operating expenses. Rental expense related to this operating lease in 2004, 2003 and 2002 was approximately $40,000, $41,000 and $39,000, respectively, and is included in *General and administrative expenses* in the accompanying statements of operations.

The following table summarizes the remaining non-cancelable future payments under operating leases for leased office space with initial or remaining non-cancelable lease terms in excess of one year:

| | | |
|---|---|---|
| 2005 | $ | 28,169 |
| 2006 | | 28,169 |
| 2007 | | 16,432 |
| Thereafter | | - |
| | $ | 72,770 |

## (8) Commitments and Contingencies

The Partnership, in the normal course of business, is subject to certain claims and litigation. The Partnership believes the outcome of such matters will not have a material effect on the assets, liabilities and partners' capital (deficit) of the Partnership.

The accompanying report of KPMG LLP is for sole and exclusive use of the Partnership. Further, the report of KPMG LLP is as of September 12, 2005 and KPMG LLP has carried out no procedures of any nature subsequent to that date which in any way extends that date.

KPMG

# SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2004 and 2003

(With Independent Auditors' Report Thereon)

KPMG

KPMG LLP
2500 D R Horton Tower
301 Commerce Street
Fort Worth, TX 76102

## Independent Auditors' Report

The Partners
Sid Richardson Energy Services, Ltd.:

We have audited the accompanying consolidated balance sheets of Sid Richardson Energy Services, Ltd. (a Texas Limited Partnership) and subsidiaries (the Partnership) as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in partners' capital, and cash flows, for each of the years in the three-year period ended December 31, 2004. These consolidated financial statements are the responsibility of the Partnership's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Partnership's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sid Richardson Energy Services, Ltd. and subsidiaries as of December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

September 12, 2005

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Consolidated Balance Sheets

December 31, 2004 and 2003

| Assets (note 4) | | 2004 | 2003 |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents (note 2(c)) | $ | 31,980,011 | 17,536,712 |
| Receivables: | | | |
| Trade | | 530,870 | 1,024,156 |
| Trade – affiliate (note 3) | | 54,817,311 | 54,851,884 |
| Notes and accrued interest receivable | | 11,415 | 14,063 |
| Notes and accrued interest receivable - affiliate (note 3) | | 13,960,012 | 16,143,076 |
| Total receivables | | 69,319,608 | 72,033,179 |
| Due from counterparties (note 2(f)) | | 1,362,977 | — |
| Deferred financing costs (note 4) | | 283,356 | 237,708 |
| Prepaid expenses and other current assets, net | | 978,291 | 1,245,481 |
| Total current assets | | 103,924,243 | 91,053,080 |
| Property, plant, and equipment, net: | | | |
| Land | | 12,787,081 | 12,787,081 |
| Buildings | | 1,551,604 | 1,551,604 |
| Gasoline plants and equipment | | 327,074,619 | 318,925,806 |
| Transportation equipment | | 2,056,103 | 1,523,335 |
| Construction in progress (note 2(i)) | | 14,302,611 | 3,395,236 |
| | | 357,772,018 | 338,183,062 |
| Less accumulated depreciation | | 135,133,126 | 116,924,025 |
| Net property, plant, and equipment | | 222,638,892 | 221,259,037 |
| Deferred financing costs, net of accumulated amortization of $105,839 and $99,045, respectively (note 4) | | 674,221 | 306,377 |
| Other assets (note 6) | | 2,074,843 | 2,011,316 |
| | $ | 329,312,199 | 314,629,810 |

| Liabilities and Partners' Capital | | | |
|---|---|---|---|
| Current liabilities: | | | |
| Bank overdraft | $ | 7,121,454 | 2,562,160 |
| Accounts payable – trade | | 2,171,440 | 4,892,078 |
| Accounts payable – affiliates (note 3) | | 3,337,513 | 5,420,488 |
| Current portion of long-term debt (note 4) | | 15,000,000 | 9,570,000 |
| Accrued liabilities (notes 2(m), 4 and 9) | | 52,968,706 | 47,649,751 |
| Total current liabilities | | 80,599,113 | 70,094,477 |
| Long-term debt (note 4) | | 127,500,000 | 63,430,000 |
| Other long-term liabilities (notes 5 and 9) | | 7,583,909 | 7,322,061 |
| Deferred tax liabilities, net (note 2(q)) | | 935,663 | 861,235 |
| Minority interest in subsidiaries (note 2(a)) | | 2,091,200 | 1,926,340 |
| Partners' capital | | 110,602,314 | 170,995,697 |
| Commitments and contingencies (notes 5, 7 and 9) | | | |
| | $ | 329,312,199 | 314,629,810 |

See accompanying notes to consolidated financial statements.

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Consolidated Statements of Operations

Years ended December 31, 2004, 2003 and 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Net sales - affiliate (note 3) | $ 640,829,010 | 581,365,463 | 354,066,709 |
| Net sales - other | 14,584,099 | 17,459,898 | 17,019,405 |
| Total net sales | 655,413,109 | 598,825,361 | 371,086,114 |
| Cost of sales (notes 5 and 7) | 577,490,932 | 539,146,015 | 338,727,862 |
| Cost of sales - affiliate (note 3) | 9,883,486 | 6,521,773 | 4,522,832 |
| Total cost of sales | 587,374,418 | 545,667,788 | 343,250,694 |
| Gross profit | 68,038,691 | 53,157,573 | 27,835,420 |
| General and administrative expenses, net (notes 3, 5, 7 and 8) | 12,406,220 | 11,279,021 | 10,398,927 |
| Income from operations | 55,632,471 | 41,878,552 | 17,436,493 |
| Other income (expense): | | | |
| Interest income - affiliate (note 3) | 266,934 | 283,316 | 565,875 |
| Interest income (note 8) | 4,903,000 | 198,958 | 34,514 |
| Interest expense (note 4) | (3,139,663) | (3,249,841) | (4,685,117) |
| Interest expense - affiliate | (126) | — | (236,701) |
| Other, net (notes 2, 4, 6 and 8) | 10,649,870 | (1,611,811) | (166,500) |
| Other income (expense), net | 12,680,015 | (4,379,378) | (4,487,929) |
| Net income before provision for income taxes and minority interest in subsidiaries' net income | 68,312,486 | 37,499,174 | 12,948,564 |
| Income tax (expense) benefit (note 2(q)) | (82,193) | (28,662) | 115,922 |
| Minority interest in subsidiaries' net income (note 2) | (142,728) | (239,349) | (93,166) |
| Net income | $ 68,087,565 | 37,231,163 | 12,971,320 |

See accompanying notes to consolidated financial statements.

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Consolidated Statements of Changes in Partners' Capital

Years ended December 31, 2004, 2003 and 2002

| | | General Partner | Limited Partner | Total |
|---|---|---|---|---|
| Balance at December 31, 2001 | $ | 1,502,252 | 134,608,962 | 136,111,214 |
| Net income (note 2) | | 129,713 | 12,841,607 | 12,971,320 |
| Balance at December 31, 2002 | | 1,631,965 | 147,450,569 | 149,082,534 |
| Distributions | | (153,180) | (15,164,820) | (15,318,000) |
| Net income (note 2) | | 372,312 | 36,858,851 | 37,231,163 |
| Balance at December 31, 2003 | | 1,851,097 | 169,144,600 | 170,995,697 |
| Distributions | | (1,284,809) | (127,196,139) | (128,480,948) |
| Net income (note 2) | | 680,876 | 67,406,689 | 68,087,565 |
| Balance at December 31, 2004 | $ | 1,247,164 | 109,355,150 | 110,602,314 |

See accompanying notes to consolidated financial statements.

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Consolidated Statements of Cash Flows

Years ended December 31, 2004, 2003 and 2002

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Net income | $ 68,087,565 | 37,231,163 | 12,971,320 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 18,243,050 | 18,654,335 | 18,237,880 |
| Amortization of deferred financing costs | 649,924 | 1,008,569 | 841,062 |
| Minority interest in subsidiaries' net income | 142,728 | 239,349 | 93,166 |
| Loss on sale of property, plant, and equipment | 19,603 | 679,155 | 132,568 |
| Deferred tax (benefit) expense | 74,428 | 19,694 | (125,359) |
| Changes in assets and liabilities: | | | |
| Trade receivables | 493,286 | 10,519 | 747,762 |
| Trade receivables – affiliate | 34,573 | (14,354,476) | (12,853,383) |
| Accrued interest receivable – affiliate | (26,711) | 30,253 | 18,116 |
| Prepaid expenses and other current assets, net | 191,170 | 32,177 | 644,038 |
| Due from counterparties | (1,362,977) | — | — |
| Other assets | (63,527) | 5,884 | (17,200) |
| Accounts payable – trade | (2,720,638) | 635,223 | (1,397,488) |
| Accounts payable – affiliates | (2,082,975) | 2,226,430 | 815,016 |
| Accrued liabilities | 5,318,955 | 12,140,356 | 17,886,464 |
| Other long-term liabilities | 261,848 | 2,574,987 | 1,708,418 |
| Net cash provided by operating activities | 87,260,302 | 61,133,618 | 39,702,380 |
| Cash flows from investing activities: | | | |
| Change in notes and accrued interest receivable | 2,648 | (14,063) | — |
| Advances on notes receivable – affiliate | (3,840,225) | (73,713,588) | (153,731,589) |
| Receipts on notes receivable – affiliate | 6,050,000 | 76,650,000 | 173,141,859 |
| Proceeds from note payable - affilate | 5,000,000 | — | 12,307,580 |
| Payments on note payable - affiliate | (5,000,000) | — | (38,562,792) |
| Purchases of property, plant, and equipment | (20,042,410) | (13,880,616) | (11,728,226) |
| Proceeds from sale of property, plant, and equipment | 475,922 | 1,481,079 | 2,454,965 |
| Net cash used in investing activities | (17,354,065) | (9,477,188) | (16,118,203) |
| Cash flows from financing activities: | | | |
| Payment of deferred financing costs | (1,063,416) | (643,130) | (514,250) |
| Bank overdraft | 4,559,294 | (1,058,940) | (236,525) |
| Proceeds on long-term debt | 80,000,000 | — | — |
| Payments on long-term debt | (10,500,000) | (22,700,000) | (18,300,000) |
| Distributions to partners | (128,480,948) | (15,318,000) | — |
| Distribution to minority interest in subsidiaries | (147,868) | — | — |
| Contribution of minority interest in subsidiaries | 170,000 | 1,050,000 | — |
| Net cash used in financing activities | (55,462,938) | (38,670,070) | (19,050,775) |
| Net change in cash and cash equivalents | 14,443,299 | 12,986,360 | 4,533,402 |
| Cash and cash equivalents at beginning of year | 17,536,712 | 4,550,352 | 16,950 |
| Cash and cash equivalents at end of year | $ 31,980,011 | 17,536,712 | 4,550,352 |

Supplemental disclosure of cash flow information:

Cash paid for interest in 2004, 2003 and 2002 totaled $2,808,335, $2,785,471 and $4,306,354, respectively.

During 2003, the Partnership sold property and equipment in exchange for $1,000,000 of common stock (other asset) and a $1,000,000 note receivable (other asset). See note 6.

See accompanying notes to consolidated financial statements.

**(1) Organization and Description of Business**

Sid Richardson Energy Services, Ltd. (the Partnership) was formed on March 1, 1993 as a Texas limited partnership under the name Sid Richardson Gasoline, Ltd. In March 2001, the Partnership changed its name to Sid Richardson Energy Services, Ltd.

The Partnership is engaged in the gathering, transmission, treating, processing and redelivery of natural gas and natural gas liquids in Texas and New Mexico. The Partnership's activities primarily include connecting the wells of natural gas producers to the Partnership's gathering systems, treating natural gas to remove impurities to ensure that it meets pipeline quality specifications, processing natural gas for the removal of natural gas liquids, transporting natural gas, and redelivering natural gas and natural gas liquids to a variety of markets. Substantially all of the Partnership's sales are made to Richardson Energy Marketing, Ltd. (REM), an affiliate under common control (note 3).

**(2) Summary of Significant Accounting Policies and Practices**

***(a) Basis of Presentation and Consolidation***

The accompanying consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America. Net income or loss is credited or charged to the partners' capital accounts in accordance with their respective percentage interest as stated in the partnership agreement. The Partnership is permitted to make distributions based on the availability of distributable funds as determined by the General Partner. The allocation of distributions is based on each partner's interests pursuant to the partnership agreement, consistent with the allocation of net income or loss.

The accompanying consolidated financial statements include the Partnership, SRCG West Texas Gathering, Inc. (SRCG West Texas) and subsidiary; Leapartners, L.P., its 99% owned subsidiary partnership (Leapartners); Mi Vida Genpar, LLC; and Sid Richardson Pipeline, Ltd. and subsidiaries (collectively the Partnership).

During 2003, the Partnership and a third party contributed certain assets to a new subsidiary partnership (Grey Ranch). The Partnership exercises control over Grey Ranch and has therefore included the assets, liabilities, income and expenses of Grey Ranch in the accompanying consolidated financial statements.

The net assets of the minority interests in Leapartners and Grey Ranch and their respective share of income and expenses are included in *Minority interest in subsidiaries* and *Minority interest in subsidiaries' net income* in the accompanying consolidated financial statements.

All significant intercompany balances and transactions have been eliminated in consolidation.

***(b) Use of Estimates***

The Partnership has made certain estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with accounting policies generally accepted in the United States of America. Although the Partnership believes the estimates are appropriate, actual results could differ from those estimates.

*(c)* ***Cash and Cash Equivalents***

The Partnership considers all highly liquid financial instruments with original maturities of three months or less to be cash equivalents. Cash and cash equivalents include \$31,363,128 and \$17,520,762 of money market investments at December 31, 2004 and 2003, respectively.

*(d)* ***Significant Customers and Concentrations of Credit Risk***

For the years ended December 31, 2004, 2003 and 2002, sales to REM, an affiliate under common control, accounted for 98%, 97% and 95% of total net sales, respectively. The Partnership believes that it could replace sales to REM with sales to other energy marketers or end users without a material adverse effect on the Partnership's results of operations.

Financial instruments, which potentially subject the Partnership to concentrations of credit risk, consist primarily of trade accounts receivable and derivative financial instruments. The Partnership's primary customer is REM. Consequently, matters affecting the business and financial condition of REM, including its operations, management, customers, and vendors, have the potential to impact the Partnership's credit exposure. The Partnership believes the risk is limited since REM's customers represent a broad and diverse group of energy marketers and end users. In addition, the Partnership's management continually monitors and reviews credit exposure to each of REM's counterparties.

*(e)* ***Reserves for Uncollectible Receivables***

The Partnership records reserves for uncollectible accounts on a specific identification basis since there is not a large volume of late paying customers. No reserves were recorded as of December 31, 2004 and 2003.

*(f)* ***Derivatives***

The Partnership periodically manages its exposure to commodity price fluctuations using derivative financial instruments. The Partnership accounts for derivative financial instruments in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended (SFAS No. 133). Derivative financial instruments subject the Partnership to off-financial statement risk. Derivative financial instruments involve not only the risk of dealing with counterparties and their ability to meet the terms of the contracts but also the risk associated with unmatched positions and market fluctuations. Notional, face or contract amounts often are used to express the volume of these transactions, but the amounts potentially subject to credit risk are much smaller.

Under SFAS No. 133, the Partnership is required to record derivative financial instruments at fair value. The fair value of derivative financial instruments is determined by commodity exchange prices, over-the-counter quotes, volatility, time value, counterparty credit and the potential impact on market prices of liquidating positions in an orderly manner over a reasonable period of time under current market conditions. The majority of the Partnership's fair values are based on actual market prices. Under SFAS No. 133, market value changes result in a change in the fair value of derivative financial instruments. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding it. If the derivative instrument does not qualify or is not designated as part of a hedging relationship, changes in fair value of the derivative are recognized in earnings as they occur. Commodity price volatility may have a significant impact on the gain or loss in any given period.

The Partnership periodically enters into certain commodity collar arrangements (commodity collars) in order to hedge against significant market value declines in commodity prices. Commodity collars are arrangements in which the counterparty agrees to be a put option seller and a call option buyer and the Partnership agrees to be the corresponding put option buyer and call option seller. Both the put option and call option are for the same quantity of a derivative commodity instrument.

At December 31, 2004, the Partnership had open commodity collars that expire on dates ranging from January 2005 to October 2006 with a net market value of $1,362,977. The Partnership has marked these derivatives to market in *Other, net* in the accompanying consolidated statements of operations as such instruments did not qualify for hedge accounting. There were no open collars at December 31, 2003 and 2002.

During 2004, 2003 and 2002, no collars were terminated or expired, and therefore, no realized gains or losses were recognized by the Partnership.

*(g)* ***Contracts for Physical Purchases and Sales***

The Partnership's contracts for the physical purchase and sale of natural gas and natural gas liquids are derivatives under SFAS No. 133, since the underlying natural gas and natural gas liquids are commodities readily convertible to cash – thereby meeting the net settlement provision of SFAS No. 133. However, the contracts do not provide for a net settlement in cash, nor do they provide for any settlement mechanism other than the physical delivery of the underlying natural gas and natural gas liquids. These contracts would therefore have qualified for the normal purchases and normal sales exemption under SFAS No. 133 had the Partnership documented its designation of the contracts as normal purchases and normal sales. In this case, the contracts would have been exempt from fair value accounting treatment and not treated as derivatives. Since the Partnership's accounting records historically have been prepared on the accrual basis of accounting in accordance with practices permitted for income tax purposes, the Partnership had not met the documentation requirements of SFAS No. 133. Since the Partnership's contracts for the physical purchase and sale of natural gas and natural gas liquids are based on a floating index price, no mark-to-market adjustment is required. Accordingly, such contracts are reported at fair value in the accompanying consolidated financial statements.

*(h)* ***Property, Plant and Equipment***

Property, plant and equipment are recorded at cost. The Partnership charges repairs and maintenance against income when incurred and capitalizes renewals and betterments, which extend the useful life or expand the capacity of the assets. The Partnership calculates depreciation on the straight-line method over the following estimated useful lives: buildings – 20 to 35 years; gasoline plants and equipment – 15 to 25 years; transportation equipment - 3 years.

*(i)* ***Capitalization of Interest***

The Partnership capitalizes interest on major projects during extended periods which are required to prepare the assets for their intended use. Such interest is allocated to property, plant and equipment and amortized over the estimated useful lives of the related assets. During 2004, 2003 and 2002, the Partnership capitalized $202,000, $87,000 and $100,000, respectively, of interest on construction in progress.

*(j)* ***Impairment of Long-Lived Assets***

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Partnership evaluates its long-lived assets for impairment when events or changes in circumstances indicate, in the Partnership's judgment, that the carrying value of such asset may not be recoverable. The determination of whether impairment has occurred is based on the Partnership's estimate of undiscounted future cash flows attributable to the assets as compared to the carrying value of the assets. If impairment has occurred, the amount of impairment recognized is determined by estimating the fair value of the assets and recording a provision for the amount by which the carrying value exceeds fair value. For assets identified to be held for sale, the carrying value of these assets is compared to the estimated fair value, less the cost to sell, to determine if impairment is required. An asset is no longer depreciated while it is held for sale. Until the assets are disposed of, an estimate of the fair value is re-evaluated when related events or circumstances change.

When determining whether impairment of one of the Partnership's long-lived assets has occurred, the Partnership must estimate the undiscounted cash flows attributable to its assets or asset groups. Such an estimate of cash flows is based on assumptions regarding future natural gas liquids product and natural gas prices. Projections of future commodity prices are inherently subjective and contingent upon a number of factors, many of which are difficult to forecast. Any significant variance in any of these assumptions or factors could materially affect future cash flows. The Partnership has reviewed its long-lived assets for impairments and has not identified any such impairments.

*(k)* ***Asset Retirement Obligation***

SFAS No. 143, *Accounting for Asset Retirement Obligations*, (SFAS No. 143) was issued in June 2001. The Partnership adopted SFAS No. 143 beginning January 1, 2003. This statement requires entities to record the fair value of a liability for legal obligations associated with the retirement obligations of tangible long-lived assets in the period in which the obligation is incurred and can be reasonably estimated. When the liability is initially recorded, a corresponding increase in the carrying amount of the related long-lived asset is recorded. Over time, accretion of the liability is recognized each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss on settlement.

Under the implementation guidelines of SFAS No. 143, the Partnership has reviewed its long-lived assets and lease arrangements for asset retirement obligation (ARO) liabilities and identified any such liabilities. These liabilities include AROs related to (i) rights-of-way and easements over property not owned by the Partnership, (ii) leases of certain currently operated facilities and (iii) regulatory requirements triggered by the abandonment or retirement of certain of these assets.

The Partnership's rights under its easements are renewable or perpetual and retirement action, if any, is required only upon non-renewal or abandonment of the easements. The Partnership currently expects to continue to use or renew all such easement agreements and to use these properties for the foreseeable future. Similarly, under certain leases of currently operated facilities, retirement action is only required upon termination of these leases and the Partnership does not expect termination in the foreseeable future. Accordingly, the Partnership is unable to reasonably estimate and record liabilities for its obligations that fall under the provisions of SFAS No. 143 because it does not believe that any of the applicable assets will be retired or abandoned in the foreseeable future. The Partnership will record AROs in the period in which the obligation may be reasonably estimated.

### *(l) Deferred Financing Costs*

Deferred financing costs are amortized on a straight-line basis over the term of the related obligations, which approximates the effective interest method. In the event the Partnership's long-term debt is refinanced or restructured, any remaining related unamortized deferred financing costs are expensed.

### *(m) Accrued Liabilities*

Accrued liabilities at December 31, 2004 and 2003 primarily consist of amounts due to producers under gas plant settlement agreements.

### *(n) Contingencies and Environmental Costs*

The Partnership records a liability for loss contingencies arising from claims, assessments, litigation, fines, and penalties in the consolidated financial statements when a loss is known or considered probable and the amount can be reasonably estimated. The Partnership reviews these estimates each accounting period as additional information is known and adjusts the loss accrual when appropriate. If the loss is not probable or cannot be reasonably estimated, a liability is not recorded in the consolidated financial statements.

Environmental expenditures are expensed or capitalized as appropriate, depending on the nature of the expenditures and their future economic benefit. Expenditures that relate to an existing condition caused by past operations that do not contribute to current or future revenue generation are expensed. Liabilities for these expenditures are recorded on an undiscounted basis (or discounted when the obligation can be settled at fixed and determinable amounts) when environmental assessments or clean-ups are probable and the costs can be reasonably estimated.

### *(o) Fair Value of Financial Instruments*

The Partnership has estimated the fair value of the Partnership's financial instruments using available market information and valuation methodologies. Considerable judgment is required to develop the estimates of fair value. Estimates of fair value are not necessarily indicative of the amount the Partnership could realize upon the sale or refinancing of such financial instruments.

The carrying amounts of cash and cash equivalents, trade receivables, accounts payable, and accrued liabilities approximate fair value due to the short-term maturities of these assets and liabilities. Derivative financial instruments are included in assets or liabilities at fair value. The carrying amounts of notes and accrued interest receivable – affiliates approximate their fair value as such instruments bore interest at a floating rate which is believed to be comparable to those rates currently offered on deposits under a centralized cash management program offered by third party financial institutions (note 3). The fair value of other assets approximates its carrying value as the underlying instruments either (i) bear interest at a rate which is believed to be comparable to those currently offered on similar subordinated instruments or (ii) are carried at values which are believed to approximate a market value for similar equity investments in private companies (note 6). The fair value of the Partnership's long-term debt and accrued interest payable is believed to approximate its carrying value as such instruments bear interest at a floating rate which was comparable to rates currently offered to the Partnership for similar debt instruments of comparable maturities by the Partnership's bankers.

***(p) Revenue Recognition***

The Partnership recognizes revenue for natural gas and natural gas liquid product sales at the time the product is delivered and title is transferred. Gas gathering, processing and treating revenues are recognized in the period in which services are provided.

***(q) Income Taxes***

The Partnership is not a taxable entity for Federal income tax purposes. As such, the Partnership does not directly pay Federal income tax. The Partnership's taxable income or loss, which may vary substantially from the net income or loss reported in the consolidated statements of operations, is includable in the Federal income tax return of each partner.

The Partnership's wholly owned subsidiary, SRCG West Texas, files consolidated Federal and state income tax returns. SRCG West Texas accounts for income taxes in accordance with the provisions of SFAS No. 109, *Accounting for Income Taxes*. This statement requires SRCG West Texas to recognize deferred tax assets and liabilities under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

During 2004, 2003 and 2002, SRCG West Texas recognized current tax expense of $7,765, $8,968 and $9,437, respectively, and deferred tax expense (benefit) of $74,428, 19,694 and $(125,359), respectively. A reconciliation of the provision for taxes for SRCG West Texas is as follows:

| | | 2004 | 2003 | 2002 |
|---|---|---|---|---|
| Expected Federal taxes at statutory rate (35%) | $ | 74,831 | 18,842 | (125,359) |
| State income taxes, net | | 7,765 | 8,968 | 9,437 |
| Other, net | | (403) | 852 | - |
| Income tax expense (benefit) | $ | 82,193 | 28,662 | (115,922) |

The principal components of SRCG West Texas' net deferred tax liabilities at December 31, 2004 and 2003 are as follows:

| | | 2004 | 2003 |
|---|---|---|---|
| Deferred income tax assets: | | | |
| Net operating loss carryforwards | $ | 467,589 | 464,759 |
| Amounts accrued for financial reporting purposes not yet deductible for tax purposes | | 79,520 | 77,381 |
| Total deferred income tax assets | | 547,109 | 542,140 |
| Less: Valuation allowance | | - | - |
| Net deferred tax assets | | 547,109 | 542,140 |
| Deferred income tax liabilities: | | | |
| Property, plant and equipment | | (1,482,772) | (1,403,375) |
| Deferred tax liabilities, net | $ | (935,663) | (861,235) |

At December 31, 2004, SRCG West Texas has net operating loss carryforwards for Federal income tax purposes of $1,335,969 which are available to offset future Federal taxable income, if any, through 2024. In assessing the realizability of deferred tax assets related to such net operating loss carryforwards, the Partnership considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the ability of SRCG West Texas to generate taxable income during the periods in which those temporary differences become deductible. The Partnership considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon projections of future taxable income, the Partnership believes it is more likely than not that SRCG West Texas will realize the benefits of these deductible differences. Therefore, no valuation allowance has been established. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced.

*(r)* ***Defined Benefit Plans***

The Partnership has a defined benefit retirement plan covering substantially all of its employees and also has a nonqualified defined benefit plan covering certain key executives. The benefits under both plans are based upon years of service and compensation during the ten calendar years before employment ceases. The Partnership computes pension expense for the defined benefit retirement plan and costs associated with the nonqualified defined benefit plan in accordance with SFAS No. 87, *Employers' Accounting for Pensions*.

*(s)* ***Recently Issued Accounting Standards***

In November 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 151, *Inventory Costs* (SFAS No. 151). This statement amends the guidance in Accounting Research Bulletin No. 43 to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material. SFAS No. 151 requires that abnormal amounts of those items be recognized as current-period charges regardless of whether they meet the criteria set forth in the earlier accounting guidance. The statement is effective for fiscal years beginning after June 15, 2005 but earlier adoption is permitted. The adoption of SFAS No. 151 is not expected to have a significant impact on the Partnership's consolidated financial statements.

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets* (SFAS No. 153). This statement amends the guidance in Accounting Principles Board opinion No. 29 to require that all exchanges of nonmonetary assets be recorded at the fair value of the assets exchanged except where a nonmonetary exchange has no commercial substance. The statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The adoption of SFAS No. 153 is not expected to have a significant impact on the Partnership's consolidated financial statements.

In March 2005, the FASB issued FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143* (FIN 47), which clarifies the accounting for conditional asset retirement obligations as used in SFAS No. 143, *Accounting for Asset Retirement Obligations*. A conditional asset retirement obligation is an unconditional legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of an entity. An entity is required to recognize a liability for the fair value of a conditional asset retirement obligation under SFAS No. 143 if the fair value of the liability can be reasonably estimated. FIN 47 permits, but does not require, restatement of interim financial information. The provisions of FIN 47 are effective for reporting periods ending after December 15, 2005. The Partnership has not yet assessed the impact of adopting FIN 47 on its consolidated financial statements.

*(t)* ***Comprehensive Income***

Comprehensive income includes net income and other comprehensive income (loss), which may include items such as unrealized holding gains and losses on available-for-sale securities, gains and losses on derivative financial instruments accounted for as a cash flow hedge, adjustments to minimum pension liabilities, or foreign currency translation adjustments. The Partnership did not have any items resulting in a difference between net income and other comprehensive income (loss) during the years ended December 31, 2004, 2003 and 2002.

**(3) Related Party Transactions**

The Partnership sells substantially all of its gas and natural gas liquids to REM, an affiliate under common control. Such sales accounted for 98%, 97% and 95% of the Partnership's total net sales during 2004, 2003 and 2002, respectively. During the Partnership's normal business cycle, these amounts are recorded as sales and are reported as *Net sales – affiliate* in the accompanying consolidated statements of operations. Amounts receivable from affiliates for sales of gas and natural gas liquids are included in *Trade receivables – affiliate* in the accompanying consolidated balance sheets.

The Partnership purchases a portion of its natural gas liquids from a related party. During the Partnership's normal business cycle, these amounts are recorded as cost of sales and are reported as *Cost of sales – affiliate* in the accompanying consolidated statements of operations. Amounts owed to affiliates for purchases of natural gas liquids are included in *Accounts payable – affiliates* in the accompanying consolidated balance sheets.

Certain employees of REM also provide services to the Partnership. During 2004, 2003 and 2002, the Partnership was allocated $1,317,236, $965,348 and $885,491, respectively, for its portion of these employees' salaries, benefits, pension expenses, and other related costs. Such allocations are reflected in *General and administrative expenses, net* in the accompanying consolidated statements of operations.

The Partnership shares certain common administrative services and facilities, including office space, with related parties. During 2004, 2003 and 2002, the Partnership reimbursed affiliates in the amount of approximately $3,938,000, $3,311,000 and $4,217,000, respectively, for its portion of these expenses. Such amounts are reflected in *General and administrative expenses, net* in the accompanying consolidated statements of operations.

The Partnership had unsecured notes receivable from an affiliate, due on demand and no later than dates ranging from April 15, 2008 to March 1, 2009, amounting to $13,875,262 and $16,085,045 at December 31, 2004 and 2003, respectively. Accrued interest associated with the notes amounted to $84,750 and $58,031 at December 31, 2004 and 2003, respectively. These notes bear interest at an agreed-upon variable rate of 2.6% and 1.4% at December 31, 2004 and 2003, respectively. These notes receivable are related to a centralized cash management program managed by affiliates and are reflected in *Notes and accrued interest receivable – affiliate* in the accompanying consolidated balance sheets. Interest related to these notes is reflected in *Interest income – affiliate* in the accompanying consolidated statements of income. These notes and accrued interest receivable – affiliate were repaid in full during May 2005.

**(4) Long-Term Debt**

At December 31, 2004, the Partnership has a $150,000,000 amended and restated credit agreement with a group of banks. The credit agreement bears interest at an agreed-upon variable rate (4.3% at December 31, 2004) and is secured by all assets of the Partnership. At December 31, 2004, long-term debt under this credit agreement amounted to $127,500,000 and current installments amounted to $15,000,000. This credit agreement requires principal payments of $7,500,000 every June and December until October 8, 2008 (maturity date).

At December 31, 2003, the Partnership had a $95,700,000 amended and restated credit agreement with a group of banks. The credit agreement bore interest at an agreed-upon variable rate (2.9% at December 31,

2003) and was secured by all assets of the Partnership. At December 31, 2003, long-term debt under this credit agreement amounted to $63,430,000 and current installments amounted to $9,570,000. This credit agreement required principal payments of $4,785,000 every June and December until July 31, 2006 (maturity date). This credit agreement was amended with the banks in October 2004 to the amended and restated credit agreement referred to in the previous paragraph.

The Partnership had accrued interest of $290,195 and $5,957 related to the debt at December 31, 2004 and 2003, respectively, which are included in *Accrued liabilities* in the accompanying consolidated balance sheets. During 2004, 2003 and 2002, the Partnership incurred $1,063,416, $643,130 and $514,250 respectively, in deferred financing costs in connection with the credit agreements and certain amendments and is amortizing these costs over the term of such loans. Amortization of deferred financing costs amounted to $249,120, $553,809 and $841,062 during 2004, 2003 and 2002, respectively, and is included in *Interest expense* in the accompanying consolidated statements of operations. Total write-offs of unamortized deferred financing costs due to refinancing of related debt obligations was $400,804 and $454,760 during 2004 and 2003, respectively, and is included in *Other, net* in the accompanying consolidated statements of operations.

The credit agreements contain certain financial covenants that require the maintenance of certain ratios. As of December 31, 2004 and 2003, the Partnership was in compliance with the covenants under the credit agreements.

## (5) Retirement Plans for Employees

*Defined Benefit Plans*

The Partnership participates in a single employer, as a member of a control group, defined benefit retirement plan (the Plan) which covers substantially all of its employees as well as certain employees of affiliates as defined by the Plan. The Plan is sponsored by the Partnership and certain affiliates and is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). In addition, the Partnership maintains a nonqualified defined benefit plan (the Restoration Plan) covering certain key executives.

The following table sets forth the benefit obligations, fair value of plan assets, and funded status at December 31, 2004 and 2003:

| | | Plan benefits | | Restoration Plan benefits | |
|---|---|---|---|---|---|
| | | 2004 | 2003 | 2004 | 2003 |
| Projected benefit obligation | $ | 26,486,546 | 24,728,087 | 1,221,559 | 1,225,445 |
| Fair value of plan assets | | 16,968,405 | 14,346,046 | - | - |
| Funded status | $ | (9,518,141) | (10,382,041) | (1,221,559) | (1,225,445) |
| Amounts recognized in the consolidated balance sheets consist of: | | | | | |
| Other long-term liabilities | $ | (6,223,240) | (6,058,547) | (970,669) | (763,515) |

The accumulated benefit obligation for the Plan was $17,083,557 and $15,231,053 at December 31, 2004 and 2003, respectively. The accumulated benefit obligation for the Restoration Plan was $527,469 and $537,524 at December 31, 2004 and 2003, respectively.

Net periodic benefit cost for the years ended December 31, 2004, 2003 and 2002 was as follows:

| | Plan benefits | | | Restoration Plan benefits | | |
|---|---|---|---|---|---|---|
| | 2004 | 2003 | 2002 | 2004 | 2003 | 2002 |
| Service cost | $ 2,033,249 | 1,822,820 | 1,574,797 | 119,373 | 53,868 | 64,718 |
| Interest cost | 1,545,505 | 1,434,000 | 1,333,779 | 76,590 | 35,821 | 45,098 |
| Expected return on assets | (1,147,684) | (1,175,751) | (1,287,227) | - | - | - |
| Recognized actuarial loss | 185,069 | 49,514 | - | 33,939 | (12,538) | - |
| Net periodic benefit cost | $ 2,616,139 | 2,130,583 | 1,621,349 | 229,902 | 77,151 | 109,816 |
| Net periodic benefit cost recognized in the consolidated statements of operations consists of: | | | | | | |
| Cost of sales | $ 2,062,923 | 1,702,866 | 1,365,009 | - | - | - |
| General and administrative expenses, net | 553,216 | 427,717 | 256,340 | 229,902 | 77,151 | 109,816 |
| Total | $ 2,616,139 | 2,130,583 | 1,621,349 | 229,902 | 77,151 | 109,816 |

The Partnership contributed $2,451,446 to the Plan during 2004. No amounts were contributed during 2003 and 2002. The Plan paid $1,154,635, $2,490,604 and $529,007 in benefits to its participants during 2004, 2003 and 2002, respectively.

The Partnership paid $22,747 in benefits each year to participants of the Restoration Plan during 2004, 2003 and 2002, respectively.

Weighted-average assumptions used to determine benefit obligations and net benefit cost for the years ended December 31, 2004, 2003 and 2002 were as follows:

| | Plan benefits | | | Restoration Plan benefits | | |
|---|---|---|---|---|---|---|
| | 2004 | 2003 | 2002 | 2004 | 2003 | 2002 |
| Discount rate | 5.75% | 6.25% | 6.75% | 5.75% | 6.25% | 6.75% |
| Expected long-term rate of return on plan assets | 8.00% | 8.00% | 8.00% | 0.00% | 0.00% | 0.00% |
| Rate of compensation increase | 5.00% | 5.50% | 5.50% | 5.00% | 5.50% | 5.50% |

The Plan's expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The return is based exclusively on the Plan's historical returns, without adjustments.

The Plan's investment policy governs how assets are invested. The policy is designed to maximize overall return potential while minimizing the risk of loss. The policy permits designated investment managers to invest in mutual funds, equities, bonds and debt instruments to establish a diversified investment portfolio. Asset allocations are reviewed with investment managers at least annually and more often when it appears that market trends might materially change. The weighted-average asset allocation of the Partnership's Plan assets at December 31, 2004 and 2003 was as follows:

| | Plan Assets At December 31 | |
|---|---|---|
| **Asset Category** | 2004 | 2003 |
| Equity securities | 58% | 56% |
| Debt securities | 13% | 16% |
| Other | 29% | 28% |
| Total | 100% | 100% |

The Partnership does not expect to make any contributions to the Plan during 2005.

The Plan and the Partnership on behalf of the Restoration Plan expect to pay the following benefits in future periods:

| | | Plan | Restoration Plan |
|---|---|---|---|
| Years Ending December 31: | | | |
| 2005 | $ | 780,831 | 17,060 |
| 2006 | | 1,323,529 | 6,868 |
| 2007 | | 1,052,352 | 9,259 |
| 2008 | | 1,123,909 | 11,479 |
| 2009 | | 1,054,948 | 14,900 |
| 2010 – 2014 | | 8,713,846 | 928,698 |

The expected benefits are based on the same assumptions used to measure the Partnership's benefit obligation at December 31 and include estimated future employee service. See note (3) for information regarding additional defined benefit plan cost allocations from REM.

On January 1, 2005, the Plan was amended to modify benefits for participants who did not meet certain age and service criteria as of that date. The amendments primarily reduced the benefit formula applicable to these participants, eliminated disability benefits previously provided under the Plan, and modified the payment options available for amounts earned under the Plan after December 31, 2004.

*Defined Contribution Plan*

The Partnership also has a 401(k) defined contribution plan to permit participant contributions on a pre-tax basis. This plan is also subject to the provisions of ERISA. The plan allows eligible employees to contribute up to the maximum IRS limits $13,000, $12,000 and $11,000 in 2004, 2003 and 2002, respectively. The Partnership matches the first 4% of the employee's annual compensation on a dollar for dollar basis, up to a maximum of $5,000 per year per employee. Contributions made to this plan by the Partnership in 2004, 2003 and 2002 were approximately $431,000, $413,000 and $395,000, respectively, and are included in *Cost of sales* and *General and administrative expenses, net* in the accompanying consolidated statements of operations.

### (6) Sale of Property and Equipment

During 2003, the Partnership sold property and equipment with a net book value of $3,176,430. In exchange for the property and equipment, the Partnership received 10,000 shares of PetroSource Energy Company capital stock with a value of $1,000,000 and a note receivable in the amount of $1,000,000. The note receivable bears interest at 6.0% and interest is payable on a quarterly basis beginning January 1, 2004 and continuing through October 1, 2004. Thereafter, quarterly payments of principal and accrued interest will be paid until October 1, 2011. The Partnership recognized a loss of $1,176,430 on this transaction which is included in *Other, net* in the accompanying consolidated statements of operations for the year ended December 31, 2003.

During 2004, the Partnership received $45,000 in additional capital stock in lieu of accrued interest. The capital stock and note receivable amounted to $2,045,000 and $2,000,000 at December 31, 2004 and 2003, respectively, and is included in *Other assets* in the accompanying consolidated balance sheets.

On March 4, 2005, PetroSource Energy Company converted to a limited partnership. Accordingly, the Partnership's capital stock was converted into partnership units.

## (7) Leases

The Partnership has operating leases primarily for pipeline capacity, compressors, land, office space and transportation equipment. The pipeline capacity and compressor leases contain renewal options. The Partnership is generally required to pay all costs such as maintenance, insurance and operating expenses associated with such leases. Rental expense for operating leases in 2004, 2003 and 2002 was approximately $1,306,000 $1,091,000 and $1,159,000, respectively, and is included in *Cost of sales* and *General and administrative expenses, net* in the accompanying consolidated statements of operations.

Future minimum lease payments under non-cancelable operating leases (with initial or remaining lease terms in excess of one year) are approximately:

| | | |
|---|---|---|
| Years Ending December 31: | | |
| 2005 | $ | 756,000 |
| 2006 | | 553,000 |
| 2007 | | 517,000 |
| 2008 | | 515,000 |
| 2009 | | 486,000 |

## (8) Litigation Settlement

During 2004, the Partnership received approximately $14,787,000 in connection with a litigation settlement with El Paso Natural Gas Company (El Paso). El Paso breached a non-compete agreement associated with certain New Mexico processing plants owned by the Partnership. Included in the settlement was approximately $9,771,000 of damages which are included in *Other, net*, approximately $4,549,000 of interest which is included in *Interest income*, and approximately $467,000 in reimbursed legal fees which are included as a reduction in *General and administrative expenses, net* in the accompanying consolidated statements of operations.

## (9) Commitments and Contingencies

*Legal Proceedings*

The Partnership, in the ordinary course of business, is subject to certain claims and litigation. The Partnership believes the outcome of such matters will not have a material effect on the consolidated balance sheet of the Partnership.

*Guarantees*

At December 31, 2004, an affiliate had issued approximately $2,900,000 in standby letters of credit to certain insurers in order to act as collateral for any deductible payments due under workers compensation, general liability, and auto liability policies covering the affiliate, the Partnership, and other affiliated entities. The Partnership and the other affiliated entities have agreed to reimburse the affiliate for those losses arising from their liabilities related to such deductible payments in the event the standby letters of credit are drawn upon by the insurers. If this situation occurs, the Partnership's maximum obligation would be dependent upon the ability of these affiliates to perform under this agreement. In the unlikely event these affiliates are unable to perform, the Partnership may be required to fund the total amount of such standby letters of credit.

*Environmental Matters*

The Partnership, in the ordinary course of business, is subject to certain environmental remediation assessments and clean-up efforts associated with operating its plants and equipment. The Partnership has identified several environmental remediation matters. The Partnership accounts for the estimated costs associated with these remediation efforts in accordance with AICPA Statement of Position 96-1, *Environmental Remediation Liabilities.* Accordingly, liabilities for these remediation efforts are recorded on an undiscounted basis when the environmental assessments or clean-ups are probable and the costs can be reasonably estimated.

The total estimated aggregate cost associated with such matters was $573,000 and $500,000 at December 31, 2004 and 2003, respectively, and is expected to be paid over the next three years. The aggregate undiscounted amount has been recorded in *Accrued liabilities* and *Other long-term liabilities* in the accompanying consolidated balance sheets since it represents the Partnership's best estimate of these costs and the expected payments are not considered to be fixed and reliably determinable. The cost estimate is based on technology that is expected to be used and is currently available to complete the remediation efforts. The estimate of costs and their timing of payment could change as a result of (i) changes to planned remediation efforts required by regulatory agencies, (ii) changes in technology available to complete the remediation efforts, and (iii) unforeseen circumstances existing at the site.

The accompanying report of KPMG LLP is for sole and exclusive use of the Partnership. Further, the report of KPMG LLP is as of September 12, 2005 and KPMG LLP has carried out no procedures of any nature subsequent to that date which in any way extends that date.

## SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES

**Unaudited Consolidated Balance Sheet**

**September 30, 2005**

| | | |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ | 11,059,946 |
| Receivables: | | |
| Trade | | 2,682,108 |
| Trade – affiliate | | 106,760,047 |
| Notes and accrued interest receivable | | 45,000 |
| Total receivables | | 109,487,155 |
| Deferred financing costs | | 283,356 |
| Prepaid expenses and other current assets, net | | 812,423 |
| Total current assets | | 121,642,880 |
| Property, plant, and equipment, net: | | |
| Land | | 12,787,081 |
| Buildings | | 1,551,604 |
| Gasoline plants and equipment | | 365,033,445 |
| Transportation equipment | | 2,504,715 |
| Construction in progress | | 8,931,192 |
| | | 390,808,037 |
| Less accumulated depreciation | | 149,060,406 |
| Net property, plant, and equipment | | 241,747,631 |
| Deferred financing costs, net of accumulated amortization of $212,517 | | 461,704 |
| Other assets | | 2,078,180 |
| | $ | 365,930,395 |
| **Liabilities and Partners' Capital** | | |
| Current liabilities: | | |
| Bank overdraft | $ | 5,822,610 |
| Accounts payable – trade | | 1,840,399 |
| Accounts payable – affiliates | | 4,410,237 |
| Current portion of long-term debt | | 15,000,000 |
| Due to counterparties | | 20,275,053 |
| Accrued liabilities | | 104,181,308 |
| Total current liabilities | | 151,529,607 |
| Long-term debt | | 113,571,428 |
| Other long-term liabilities | | 8,949,765 |
| Deferred tax liabilities, net | | 1,018,438 |
| Minority interest in subsidiaries | | 2,847,510 |
| Partners' capital | | 88,013,647 |
| Commitments and contingencies | | — |
| | $ | 365,930,395 |

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Unaudited Consolidated Statement of Operations

Nine Months Ended September 30, 2005

| | |
|---|---|
| Net sales - affiliate | $ 677,664,065 |
| Net sales - other | 13,655,487 |
| Total net sales | 691,319,552 |
| Cost of sales | 549,489,520 |
| Cost of sales - affiliate | 76,167,051 |
| Total cost of sales | 625,656,571 |
| Gross profit | 65,662,981 |
| General and administrative expenses, net | 11,870,872 |
| Income from operations | 53,792,109 |
| Other income (expense): | |
| Interest income - affiliate | 164,868 |
| Interest income | 691,121 |
| Interest expense | (4,853,160) |
| Interest expense - affiliate | (2,944) |
| Loss on derivative instruments, net | (21,638,030) |
| Other, net | 10,548 |
| Other income (expense), net | (25,627,597) |
| Net income before provision for income taxes and minority interest in subsidiaries' net income | 28,164,512 |
| Income tax (expense) benefit | (90,635) |
| Minority interest in subsidiaries' net income | (263,810) |
| Net income | $ 27,810,067 |

**SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES**

Unaudited Consolidated Statement of Changes in Partners' Capital

Nine Months Ended September 30, 2005

| | | General Partner | Limited Partner | Total |
|---|---|---|---|---|
| Balance at December 31, 2004 | $ | 1,247,164 | 109,355,150 | 110,602,314 |
| Distributions | | (503,987) | (49,894,747) | (50,398,734) |
| Net income | | 278,101 | 27,531,966 | 27,810,067 |
| Balance at September 30, 2005 | $ | 1,021,278 | 86,992,369 | 88,013,647 |

## SID RICHARDSON ENERGY SERVICES, LTD. AND SUBSIDIARIES

Unaudited Consolidated Statement of Cash Flows

Nine Months Ended September 30, 2005

| | |
|---|---|
| Cash flows from operating activities: | |
| Net income | $ 27,810,067 |
| Adjustments to reconcile net income to net cash provided by operating activities: | |
| Depreciation and amortization | 14,135,465 |
| Amortization of deferred financing costs | 212,517 |
| Minority interest in subsidiaries' net income | 263,810 |
| Gain on sale of property, plant, and equipment | (10,264) |
| Deferred tax (benefit) expense | 82,775 |
| Changes in assets and liabilities: | |
| Trade receivables | (2,151,238) |
| Trade receivables – affiliate | (51,942,736) |
| Accrued interest receivable – affiliate | 84,750 |
| Prepaid expenses and other current assets, net | 108,853 |
| Due from counterparties | 1,362,977 |
| Other assets | (3,337) |
| Accounts payable – trade | (331,041) |
| Accounts payable – affiliates | 1,072,724 |
| Due to counterparties | 20,275,053 |
| Accrued liabilities | 51,212,602 |
| Other long-term liabilities | 1,365,856 |
| Net cash provided by operating activities | 63,548,833 |
| Cash flows from investing activities: | |
| Change in notes and accrued interest receivable | (33,585) |
| Advances on notes receivable – affiliate | (1,183,000) |
| Receipts on notes receivable – affiliate | 15,058,262 |
| Purchases of property, plant, and equipment | (33,196,827) |
| Proceeds from sale of property, plant, and equipment | 19,902 |
| Net cash used in investing activities | (19,335,248) |
| Cash flows from financing activities: | |
| Bank overdraft | (1,298,844) |
| Payments on long-term debt | (13,928,572) |
| Distributions to partners | (50,398,734) |
| Contribution of minority interest in subsidiaries | 492,500 |
| Net cash used in financing activities | (65,133,650) |
| Net change in cash and cash equivalents | (20,920,065) |
| Cash and cash equivalents at December 31, 2004 | 31,980,011 |
| Cash and cash equivalents at September 30, 2005 | $ 11,059,946 |

Supplemental disclosure of cash flow information:
Cash paid for interest was $5,725,390 during the nine months ended September 30, 2005.

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Unaudited Balance Sheet

September 30, 2005

**Assets**

| | | |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $ | 2,322,031 |
| Receivables: | | |
| Trade | | 161,502,055 |
| Trade – affiliates | | 3,804,231 |
| Due from brokers | | 9,922,089 |
| Due from counterparties | | 4,376,970 |
| Total receivables | | 179,605,345 |
| Inventories | | 3,098,828 |
| Prepaid expenses | | 18,010 |
| Total current assets | | 185,044,214 |
| Property, plant, and equipment, at cost: | | |
| Land | | 55,523 |
| Leasehold improvements | | 107,321 |
| Pipeline equipment | | 1,471,698 |
| Office equipment | | 672,811 |
| Transportation equipment | | 29,406 |
| | | 2,336,759 |
| Less accumulated depreciation | | 1,601,883 |
| Net property, plant, and equipment | | 734,876 |
| | $ | 185,779,090 |

**Liabilities and Partners' Capital (Deficit)**

| | | |
|---|---|---|
| Current liabilities: | | |
| Bank overdraft | $ | 220,891 |
| Accounts payable – trade | | 61,943,980 |
| Accounts payable – affiliates | | 104,589,152 |
| Due to counterparties | | 4,727,916 |
| Accrued liabilities | | 1,313,275 |
| Notes and accrued interest payable - affiliates | | 8,904,239 |
| Total current liabilities | | 181,699,453 |
| Other long-term liablities | | 8,305,122 |
| Partners' capital (deficit) | | (4,225,485) |
| Commitments and contingencies | | — |
| | $ | 185,779,090 |

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Unaudited Statement of Operations

Nine Months Ended September 30, 2005

| | |
|---|---|
| Natural gas liquids and natural gas sales | $ 1,007,593,102 |
| Cost of sales | 1,006,820,942 |
| Loss on derivative instruments, net | 1,242,237 |
| General and administrative expenses | 2,538,174 |
| Operating income (loss) | (3,008,251) |
| Other income (expense): | |
| Interest income | 462,742 |
| Interest expense – affiliates | (4,239) |
| Other, net | 3,409 |
| Other income (expense), net | 461,912 |
| Net loss | $ (2,546,339) |

**RICHARDSON ENERGY MARKETING, LTD.**
(a Texas Limited Partnership)

Unaudited Statement of Changes in Partners' Capital (Deficit)

Nine Months Ended September 30, 2005

| | | General Partner | Limited Partner | Total |
|---|---|---|---|---|
| Balance at December 31, 2004 | $ | 128,267 | (1,807,412) | (1,679,145) |
| Net loss | | (25,463) | (2,520,876) | (2,546,339) |
| Balance at September 30, 2005 | $ | 102,804 | (4,328,288) | (4,225,484) |

**RICHARDSON ENERGY MARKETING, LTD.**

(a Texas Limited Partnership)

Unaudited Statement of Cash Flows

Nine Months Ended September 30, 2005

| | | |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $ | (2,546,339) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Depreciation | | 69,572 |
| Bad debt expense | | 1,887 |
| Loss on derivative instruments, net | | 266,817 |
| Changes in assets and liabilities: | | |
| Trade receivables | | (88,444,521) |
| Trade receivables – affiliates | | 3,643,842 |
| Due from counterparties | | (2,931,268) |
| Inventories | | (2,918,983) |
| Prepaid expenses | | (1,069) |
| Other assets | | 25,000 |
| Accounts payable – trade | | 42,071,026 |
| Accounts payable – affiliates | | 49,749,262 |
| Due to counterparties | | 4,375,414 |
| Accrued liabilities | | (259,678) |
| Accrued interest payable – affiliates | | 1,078 |
| Other long-term liabilities | | (658,677) |
| Net cash provided by operating activities | | 2,443,363 |
| Cash flows from investing activities: | | |
| Purchases of property, plant and equipment | | (26,263) |
| Change in due from brokers | | (9,396,125) |
| Settlement of futures, net | | (1,125,304) |
| Proceeds from sale of marketable securities | | 500 |
| Net cash used in investing activities | | (10,547,192) |
| Cash flows from financing activities: | | |
| Change in bank overdraft | | (311,026) |
| Proceeds from note payable – affiliates | | 22,903,161 |
| Payments on note payable – affiliates | | (14,000,000) |
| Net cash provided by financing activities | | 8,592,135 |
| Net change in cash and cash equivalents | | 488,306 |
| Cash and cash equivalents at December 31, 2004 | | 1,833,725 |
| Cash and cash equivalents at September 30, 2005 | $ | 2,322,031 |

Supplemental disclosure of cash flow information:

Cash paid for interest was $3,160 during the nine months ended September 30, 2005.